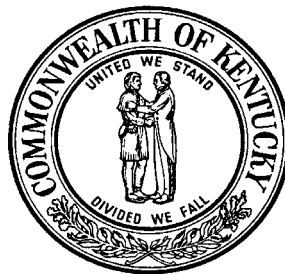


**LETTER FROM THE AUDITOR OF PUBLIC ACCOUNTS  
JUSTICE CABINET**

**In Reference to the Statewide Single Audit  
of the Commonwealth of Kentucky**

**For the Year Ended  
June 30, 2005**



**CRIT LUALLEN  
AUDITOR OF PUBLIC ACCOUNTS  
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## **TABLE OF CONTENTS**

MANAGEMENT LETTER .....	5
LIST OF APPREVIATIONS/ACRONYMS .....	3
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS .....	4
NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS .....	5
FINANCIAL STATEMENT FINDINGS .....	7
<i>Other Matters Relating to Internal Controls and/or</i>	
<i>Instances of Noncompliance</i> .....	7
FINDING 05-JUST-1: The Justice Cabinet Should Review And Enforce	
Finance And Administration Cabinet ProCard Policies And Procedures .....	7
FEDERAL AWARD FINDINGS AND QUESTIONED COSTS .....	10
<i>Reportable Conditions Relating to Internal Control and/or</i>	
<i>Reportable Instances of NonCompliance</i> .....	10
FINDING 05-JUST-2: The Justice Cabinet Should Have A Documented	
Method In Place For Allocating Indirect Charges To Their Grant Programs .....	10
FINDING 05-JUST-3: The Justice Cabinet Should Implement Procedures To	
Ensure Consistent Enforcement And Documentation Of Subrecipient	
Monitoring Requirements.....	13
FINDING 05-JUST-4: The Justice Cabinet Should Agree Federal	
Expenditure Reports To MARS .....	15
FINDING 05-JUST-5: The Justice Cabinet Should Not Supplant State	
Funds With Federal Funds.....	17
FINDING 05-JUST-6: The Justice Cabinet Should Ensure That All	
Equipment Is Properly Entered Into MARS.....	20
SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS.....	24





**CRIT LUALLEN**  
**AUDITOR OF PUBLIC ACCOUNTS**

To the People of Kentucky  
Honorable Ernie Fletcher, Governor  
Brigadier General Norman Arflak, Secretary  
Justice Cabinet

**MANAGEMENT LETTER**

KRS 43.090 (1) requires the Auditor of Public Accounts, upon completion of each audit and investigation, to prepare a report of all findings and recommendations, and to furnish copies of the report to the head of the agency to which the report pertains, and to the Governor, among others. This KRS also requires the Justice Cabinet to, within 60 days of the completion of the final audit, notify the Legislative Research Commission and the Auditor of Public Accounts of the audit recommendations it has implemented and those it has not implemented and any reasons therefore. We are providing this letter to the Justice Cabinet, Office of the Secretary in compliance with KRS 43.090.

The work completed on the Justice Cabinet, Office of the Secretary is part of the overall opinions included in the audit of the Commonwealth of Kentucky's Comprehensive Annual Financial Report (CAFR) and Statewide Single Audit of Kentucky (SSWAK). Findings and recommendations for agencies, audited as part of the CAFR and SSWAK, if applicable, can be found in the Statewide Single Audit Report. This report can be obtained on our website at [www.auditor.ky.gov](http://www.auditor.ky.gov).

In planning and performing our audits of the Commonwealth for the year ended June 30, 2005, we considered the Justice Cabinet, Office of the Secretary's internal control over financial reporting and compliance with laws, regulations, contracts and grant agreements in order to determine our auditing procedures for the purpose of expressing opinions included in the audit of the CAFR and SSWAK and not to provide an opinion on internal control or on compliance.

However, during our audit we became aware of certain matters that are opportunities for strengthening internal controls and operating efficiency. The SSWAK is a separate report dated March 9, 2006 and contains all reportable conditions and material weaknesses in the Commonwealth's internal control structure and also contains all reportable instances of noncompliance. This letter does contain the Justice Cabinet, Office of the Secretary findings and our recommendations that have been extracted from the SSWAK report along with other matters that have been identified.



To the People of Kentucky  
Honorable Ernie Fletcher, Governor  
Brigadier General Norman Arflak, Secretary  
Justice Cabinet

We will review the status of these comments during our next audit. We have already discussed many of these comments and suggestions with various Justice Cabinet, Office of the Secretary personnel, and we will be pleased to discuss them in further detail at your convenience, to perform any additional study of these matters, or to assist you in implementing the recommendations.

Included in this letter are the following:

- ◆ Acronym List
- ◆ Schedule of Expenditures of Federal Awards
- ◆ Notes to the Schedule of Expenditures of Federal Awards
- ◆ Findings and Recommendations
- ◆ Summary Schedule of Prior Year Audit Findings

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Crit Luallen", with a long horizontal flourish extending to the right.

Crit Luallen  
Auditor of Public Accounts

Audit fieldwork completed -  
March 9, 2006

**LIST OF APPREVIATIONS/ACRONYMS**

APA	Auditor of Public Accounts
CFDA	Catalog of Federal Domestic Assistance
CFR	Code of Federal Regulations
FAC	Finance and Administration Cabinet
FAP	Finance and Administration Cabinet Policies
FY	Fiscal Year
GMB	Grants Management Branch
JAG	Justice Assistance Grants
JUST	Justice Cabinet, Office of the Secretary
JV	Journal Voucher
KRS	Kentucky Revised Statutes
KSP	Kentucky State Police
KYASAP	Kentucky Agency for Substance Abuse Policy
MARS	Management Administrative Reporting System
ODCP	Office of Drug Control Policy
OMB	Office of Management and Budget
SF	Short Form
US	United States
USDOJ	United States Department of Justice
VAWA	Violence Against Women Formula Grants
VOCA	Crime Victim Assistance Grant

**JUSTICE CABINET OFFICE OF THE SECRETARY**  
**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS**  
**FEDERAL ASSISTANCE PROGRAMS**  
**FOR THE YEAR ENDED JUNE 30, 2005**

CFDA # Program Title		Expenditures		Provided to Subrecipient
		Cash	Noncash	
JUSTICE CABINET				
<u>U.S. Department of Justice</u>				
Direct Programs:				
16.550	State Justice Statistics Program for Statistical Analysis Centers	\$	55,363	
16.554	National Criminal History Improvement Program (Note 4)		-	
16.560	National Institute of Justice Research, Evaluation and Development Project Grants		31,300	
16.575	Crime Victim Assistance		4,496,696	\$ 4,353,299
16.579	Byrne Formula Grant Program		4,665,061	4,163,356
16.586	Violent Offender Incarceration and Truth in Sentencing Incentive Grants		12,642	
16.588	Violence Against Women Formula Grants (Note 3)		1,685,565	1,665,387
16.589	Rural Domestic Violence and Child Victimization Enforcement Grant Program		182,252	182,253
16.592	Local Law Enforcement Block Grants Program		190,604	181,774
16.593	Residential Substance Abuse Treatment for State Prisoners (Note 4)		-	
16.607	Bulletproof Vest Partnership Program (Note 4)		-	
<u>U.S. Department of Homeland Security</u>				
Direct Programs:				
Homeland Security Cluster:				
97.004	State Domestic Preparedness Equipment Support Program (Note 2)		47,113	
TOTAL JUSTICE CABINET OFFICE OF THE SECRETARY		\$	11,366,596	\$ 10,546,069



**NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS**  
**FOR THE YEAR ENDED JUNE 30, 2005**

**Note 1 - Purpose of the Schedule and Significant Accounting Policies**

**Basis of Presentation** - OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, requires a Schedule of Expenditures of Federal Awards showing each federal financial assistance program as identified in the *Catalog of Federal Domestic Assistance*. The accompanying schedule includes all federal grant activity for the Commonwealth, except those programs administered by state universities, and is presented primarily on the basis of cash disbursements as modified by the application of Kentucky Revised Statute (KRS) 45.229. Consequently, certain expenditures are recorded in the accounts only when cash is disbursed. The Commonwealth elected to exclude state universities from the statewide single audit, except as part of the audit of the basic financial statements.

KRS 45.229 provides that the Finance and Administration Cabinet may, “for a period of thirty (30) days after the close of any fiscal year, draw warrants against the available balances of appropriations made for that fiscal year, for the payment of expenditures incurred during that year or in fulfillment of contracts properly made during the year, but for no other purpose.” However, there is an exception to the application of KRS 45.229 in that regular payroll expenses incurred during the last pay period of the fiscal year are charged to the next year.

The basic financial statements of the Commonwealth are presented on the modified accrual basis of accounting for the governmental fund financial statements and the accrual basis of accounting for the government-wide, proprietary fund, and fiduciary fund financial statements. Therefore, the schedule may not be directly traceable to the basic financial statements in all cases.

Noncash assistance programs are not reported in the basic financial statements of the Commonwealth for FY 2005.

Clusters of programs are indicated in the schedule by light gray shading.

**Inter-Agency Activity** - Certain transactions relating to federal financial assistance may appear in the records of more than one (1) state agency. To avoid the overstatement of federal expenditures, the following policies were adopted for the presentation of the schedule:

- (a) Federal moneys may be received by a state agency and passed through to another state agency where the moneys are expended. Except for pass-throughs to state universities as discussed below, this inter-agency transfer activity is reported by the agency expending the moneys.

State agencies that pass federal funds to state universities report those amounts as expenditures.

**NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FOR THE YEAR ENDED JUNE 30, 2005  
(CONTINUED)**

**Note 1 - Purpose of the Schedule and Significant Accounting Policies (Continued)**

- (b) Federal moneys received by a state agency and used to purchase goods or services from another state agency are reported in the schedule as an expenditure by the purchasing agency only.

**Note 2 - Type A Programs**

Type A programs for the Commonwealth mean any program for which total expenditures of federal awards exceeded \$20 million for FY 2005. The Justice Cabinet, Office of the Secretary had no programs that met the Type A program definition for the year ended June 30, 2005.

**Note 3 - Violence Against Women Formula Grants (CFDA #16.588)**

An audit of the Administrative Office of the Courts by the Kentucky Justice and Public Safety Cabinet resulted in \$100.97 being determined unallowable and being returned to the Kentucky Justice and Public Safety Cabinet.

**Note 4 - Zero Expenditure Programs**

These programs had no expenditures related to the Justice Cabinet Office of the Secretary during FY 2005. The zero expenditure programs included programs with no activity during the year, such as old programs not officially closed out or new programs issued late in the fiscal year. They also included programs with activity other than expenditures.

**FINANCIAL STATEMENT FINDINGS*****Other Matters Relating to Internal Controls and/or  
Instances of Noncompliance*****FINDING 05-JUST-1: The Justice Cabinet Should Review And Enforce Finance And Administration Cabinet ProCard Policies And Procedures**

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During our testing of ProCard transactions at the Justice and Public Safety Cabinet's Office of the Secretary, a cardholder informed us that he had shared his ProCard number with a coworker so that the co-worker could make purchases with his card. The cardholder stated this was necessary because the one (1) ProCard issued to his agency was not sufficient to meet the purchasing needs of his agency.

Auditors also found that four (4) finance charges were paid during FY 2005, which indicates that balances had not been paid in full in a timely manner as required by the Finance and Administration Cabinet's ProCard policy.

There is currently only one card issued for the Medical Examiners office and the cardholder reported that this was inadequate to serve the needs of that office.

Card sharing places purchasing responsibilities with someone not approved by the cabinet to make ProCard purchases and unfamiliar with ProCard policies and procedures. This practice also places the cardholder in the position of being responsible for unauthorized purchases made by the card sharer.

Late payments are unnecessary expenses that should not be incurred by state agencies.

Card sharing is specifically prohibited for cards issued to individuals by Finance policies and procedures.

FAP 111-58-00 (2) states, "An individual card embossed with an employee's name shall be used exclusively by that employee and shall not be shared or loaned to other employees."

FAP 111-58-00 (17) (g) states, "Each agency shall take appropriate disciplinary actions whenever any violation of this policy is identified. For the first substantiated violation, the agency shall, at a minimum, issue an appropriate reprimand, including specific notice that a second violation will result in revocation of card privileges and further potential disciplinary action up to and including dismissal. Any substantiated second violation within two (2) years if the first violation shall automatically result in revocation of card privileges, in addition to further disciplinary action as warranted. Any violation that involves the use of the card for personal purposes shall require the agency to collect reimbursement of the charge, along with revocation of card privileges and disciplinary action as either or both may be deemed appropriate under the circumstances."

FAP 111-58-00 (19) states, "An agency shall process payments in the state's procurement system in sufficient time to pay the issuing bank. If authorization is not received in sufficient time, the agency shall be responsible for payment of interest charges."

## FINANCIAL STATEMENT FINDINGS

### *Other Matters Relating to Internal Controls and/or Instances of Noncompliance*

#### **FINDING 05-JUST-1: The Justice Cabinet Should Review And Enforce Finance And Administration Cabinet ProCard Policies And Procedures (Continued)**

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##### **Recommendation**

Since the Justice Cabinet has been made aware of the improper use of a ProCard, we recommend they review FAP 111-58-00 (17) (g) which requires appropriate disciplinary action when FAC ProCard policy is violated. The ProCard administrator should review ProCard policies with all cardholders including FAP 111-58-00, and require their compliance.

The ProCard administrator should ensure that payments to the bank are processed timely.

The Justice Cabinet should proceed with their plan to issue additional cards within the Medical Examiner's office to meet their purchasing needs.

##### **Management's Response and Corrective Action Plan**

*The Office of Management and Administrative Services within the Justice and Public Safety Cabinet acknowledges the validity of the finding that an individual's pro card had been used by another staff member other than himself; however, the basis of the occurrence(s) was due to operational circumstances, not to be considered as routine activity.*

*Factors include the following:*

1. *An additional card had been obtained for use by the Medical Examiner's Office which remained in the possession of the pro-card administrator until the necessary training and instruction could be given to the identified 'new card holder'. (Upon receipt of the card, soon to be changes had been announced by both the pro card program (Finance) as well as proposed changes within the agency. Therefore, until such time the pro-card administrator could be properly trained and instructed of the necessary changes, she was unable to adequately instruct the new card holder of all policies and procedures that governed the program.*
2. *Each/any occurrence of card activity initiated by a second party is reflective of an in-house transaction (telephone). The card was never taken from the Medical Examiner's Office.*
3. *Prior authorization by the assigned card holder was granted for use in each/every occurrence.*

**FINANCIAL STATEMENT FINDINGS*****Other Matters Relating to Internal Controls and/or  
Instances of Noncompliance*****FINDING 05-JUST-1: The Justice Cabinet Should Review And Enforce Finance And  
Administration Cabinet ProCard Policies And Procedures (Continued)**

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**Management's Response and Corrective Action Plan (Continued)**

4. *Due to the nature of various requested laboratory testing within the Toxicology Section of the Medical Examiner's Division, the immediate purchase of certain chemicals and supplies became of critical importance in order to allow the Toxicology laboratory to meet deadlines of providing laboratory results to coroners and law enforcement officers for court related cases.*

*The Office of Management and Administrative Services further acknowledges the validity of the finding of four finance charges during FY 05. With the recent development of programmatic changes, additional internal controls and the training of additional staff, inclusive of 'all areas' of the Pro-card program, the pro-card administrator seeks to achieve and maintain a status of compliance with payment activity. This will eliminate the addition of any late payment fee within the circumstances of which the agency has control.*

**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Reportable Conditions Relating to Internal Control and/or  
Reportable Instances of NonCompliance*****FINDING 05-JUST-2: The Justice Cabinet Should Have A Documented Method In Place For Allocating Indirect Charges To Their Grant Programs**

---

State Agency: Justice Cabinet - Office of the Secretary

Federal Program: CFDA 16.575--Crime Victim Assistance

CFDA 16.579--Byrne Formula Grant Program

CFDA 16.588--Violence Against Women Formula Grants

Federal Agency: U.S. Department of Justice - Office of Justice Programs

Pass-Through Agency: Not Applicable

Compliance: Allowable Costs/Cost Principles

Amount of Questioned Costs: \$372,757

Indirect costs are those costs that benefit common activities and, therefore, cannot be readily assigned to a specific direct cost objective or project. Since the FY 2002 audit, we have questioned the indirect costs charged to the above listed federal grants because there was not an approved indirect cost allocation plan as required by the Financial Guide.

During the 2005 fiscal year, Grants Management Branch (GMB) submitted an indirect cost allocation plan. The US Department of Justice (USDOJ) Office of Justice Programs reviewed the proposal and determined that GMB was not required to have an approved indirect cost allocation plan.

In order to resolve this matter, we contacted the USDOJ twice and reviewed correspondence in this matter. Although USDOJ determined that the minimal indirect costs charged to the grant did not require a formal indirect cost plan, Federal guidelines still require documentation of expenditures and a method of allocating those charges to the grant other than those charges directly allocable to the grant.

In the absence of an approved indirect cost rate, the GMB should have a documented methodology in place for allocating indirect charges to their grant programs. As the auditor has documented since FY 2002, there is not a formal method for allocating indirect costs among the grants administered by GMB. Therefore, we question all administrative costs charged to the three (3) grants audited in FY 2005, \$80,830.

As auditors found in the FY 2004, the Justice Cabinet allocated FY 2005 payroll expenditures to the grants indirectly using percentages determined in a time study from several years ago, which could not be documented. We do not question that GMB employees have worked directly on the grant; rather, the method used to allocate their expenses to the various grants. Their allocation method is indirect because it was not based on actual time or effort reports (i.e., timesheet). Therefore, we question all salary and related charges to each of the three (3) grants audited for FY 2005, \$291,927. Indirect expenses and payroll, which were charged to the grants without a documented basis of allocation, are not allowable expenditures.

**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Reportable Conditions Relating to Internal Control and/or Reportable  
Instances of NonCompliance*****FINDING 05-JUST-2: The Justice Cabinet Should Have A Documented Method In  
Place For Allocating Indirect Charges To Their Grant Programs (Continued)**

According to the US Department of Justice Financial Guide Chapter 7, Allowable Costs, the salaries of employees working directly with grant programs is allowable. “Where salaries apply to execution of two or more grant programs, cost activities, project periods, and/or overlapping periods, proration of costs to each activity must be made based on time and/or effort reports. In cases where two or more grants constitute one identified activity or program, salary charges to one grant may be allowable after written permission is obtained from the awarding agency. Salary supplements, including severance provisions and other benefits with non-Federal funds, are prohibited without approval of the awarding agency. (Refer to OMB Circular A-87, Attachment B, OMB Circular A-122, or OMB Circular A-21).”

Allowable costs are those costs identified in the circulars and in the grant program's authorizing legislation. In addition, costs must be reasonable, allocable, necessary to the project, and comply with the funding statute requirements.

The A-133 Compliance Supplement Part 3 states that allowable costs must be allocable to the Federal award it is charged. “A cost is allocable to a particular cost objective (e.g., a specific function, program, project, department, or the like) if the goods or services involved are charged or assigned to such cost objective in accordance with relative benefits received.”

**Recommendation**

We recommend that the Justice Cabinet GMB begin the process of documenting their methodology for charging indirect expenditures such as rent and utilities among the various grants that they administer. They should also make arrangements with the US Department of Justice to repay the \$372,757 in questioned costs for fiscal year 2005.

During FY 2005, GMB personnel worked on new procedures for documenting employee hours worked on grants in order to directly charge their actual hours worked on each grant accordingly. This plan was implemented in July 2005 and was not in place during FY 2005.

We commend GMB for the development of their system for documenting payroll expenditures. While not in place for the 2005 fiscal year, this new system was in place within three (3) months after the completion of the 2004 fiscal year audit.

**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Reportable Conditions Relating to Internal Control and/or Reportable  
Instances of NonCompliance*****FINDING 05-JUST-2: The Justice Cabinet Should Have A Documented Method In  
Place For Allocating Indirect Charges To Their Grant Programs (Continued)****Management's Response and Corrective Action Plan (Continued)**

*Although documentation of previous facilities costs allocations was lacking, GMB was charged a proportional cost of the Cabinet's space and utilities costs that was based on established Finance and Administration Cabinet rates and assigned square footage. These costs were subsequently distributed among the grants reviewed, and others. In FY 2005, GMB was officed in an enclosed space, unused by other Cabinet staff or functions, so all charges reflected GMB use only.*

*In its continuing efforts to improve documentation and operations, the Justice and Public Safety Cabinet and GMB had already made plans to revise its facilities costs allocations prior to the receipt of this finding. Similar to the time study, an assessment will be undertaken to establish current allocable costs, and will be applied to all FY 2006 and future costs. The methodology will be appropriately documented. We are still awaiting guidance from our cognizant federal agency, U.S. Department of Justice, on prior years' (FY 2003 and 2004) indirect audit cost findings, and will follow their directives as previously stated for all affected years.*

**Auditor's Reply**

We encourage the Justice Cabinet to follow through with their plans to document their method of allocating indirect costs for FY 2006 and future years and follow U.S. Department of Justice Guidance regarding indirect cost. However, the Justice Cabinet has not documented their method for allocating indirect charges among grants in FY 2003, 2004, or 2005. Without this documentation we are not able to determine if charges were allocated in agreement with federal requirements. Therefore, we continue to question these costs.



## **FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

### ***Reportable Conditions Relating to Internal Control and/or Reportable Instances of NonCompliance***

#### **FINDING 05-JUST-3: The Justice Cabinet Should Implement Procedures To Ensure Consistent Enforcement And Documentation Of Subrecipient Monitoring Requirements**

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State Agency: Justice Cabinet - Office of the Secretary

Federal Program: CFDA 16.575--Crime Victim Assistance

CFDA 16.579--Byrne Formula Grant Program

CFDA 16.588--Violence Against Women Formula Grants

Federal Agency: U.S. Department of Justice - Office of Justice Programs

Pass-Through Agency: Not Applicable

Compliance: Subrecipient Monitoring

Amount of Questioned Costs: None

Grants Management Branch (GMB) policies require subrecipients of federal grants they administer to submit quarterly financial reports 15 days after the end of the quarter. GMB has not enforced this requirement; testing of subrecipient financial reports indicates that reports were consistently submitted late and in some cases not at all for subrecipients of the three (3) grant programs listed above. Furthermore, there was no consistent enforcement or documentation of the subrecipient reporting requirements.

While testing subrecipient files of the BYRNE grant, we found that subrecipient financial reports had not been submitted timely nor was there any evidence that GMB had reviewed or approved the payments to the following grantees: Office of Drug Control Policy (\$51,795), Kentucky Parole Board (\$217,856), and Kentucky State Police (\$1,210,614). These grantees are all within the Justice and Public Safety Cabinet and participate in MARS project billing. Each had received reimbursement for their expenditures without review.

For the VAWA grant, GMB did not consistently document their determination of the subrecipient's requirement to obtain an A-133 audit, or their review of required A-133 subrecipient audits and/or audit findings.

During FY 2005, GMB did not perform sufficient monitoring activities or document that subrecipients were using federal awards in compliance with the applicable laws, regulations, and the provisions of grant agreements. Subrecipients could be in noncompliance with federal requirements and grant funds could be spent erroneously when monitoring is not performed adequately or timely.

Office of Justice Programs Financial Management Guide, Chapter 19: AUDIT OF SUBRECIPIENTS states, "When subawards are made to another organization or organizations, the recipient shall require that subrecipients comply with the audit requirements set forth in this chapter. Recipients are responsible for ensuring that

**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Reportable Conditions Relating to Internal Control and/or Reportable  
Instances of NonCompliance*****FINDING 05-JUST-3: The Justice Cabinet Should Implement Procedures To Ensure  
Consistent Enforcement And Documentation Of Subrecipient Monitoring  
Requirements (Continued)**

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subrecipient audit reports are received and for resolving any audit findings. Known or suspected violations of any law encountered during audits, including fraud, theft, embezzlement, forgery, or other serious irregularities, must be communicated to the recipient. For subrecipients who are not required to have an audit as stipulated in OMB Circular A-133, the recipient is still responsible for monitoring the subrecipients' activities to provide reasonable assurance that the subrecipient administered Federal awards in compliance with Federal requirements.”

OMB Circular A-133 (d) “Pass-through entity responsibilities. A pass-through entity shall perform the following for the Federal awards it makes: (3) Monitor the activities of subrecipients as necessary to ensure that Federal awards are used for authorized purposes in compliance with laws, regulations, and the provisions of contracts or grant agreements and that performance goals are achieved. (4) Ensure that subrecipients expending \$300,000 (\$500,000 for fiscal years ending after December 31, 2003) or more in Federal awards during the subrecipient's fiscal year have met the audit requirements of this part for that fiscal year.”

**Recommendation**

We recommend that GMB implement procedures for monitoring the timely submission of subrecipient financial and programmatic reports.

We also recommend that GMB update procedures to ensure consistent enforcement and documentation of A-133 audit requirements for all subrecipients.

**Management's Response and Corrective Action Plan**

*The Justice and Public Safety Cabinet substantially agrees with the finding and has completed, or will institute, steps to resolve the issues identified. Due to the volume of total transactions, KSP was allowed to establish Byrne grants as “participating” in MARS; however, quarterly financial reports were required and reviewed, with necessary adjustments made upon completion of review. This reimbursement method will no longer be available to state agency subgrantees as Byrne funds are replaced with Justice Assistance Grant funds. JAG subgrants were set up to require reimbursement upon approval, rather than automatically with subsequent review, due to the upfront receipt of funds from U.S. Department of Justice, rather than the traditional drawdown method previously used.*

## **FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

### ***Reportable Conditions Relating to Internal Control and/or Reportable Instances of NonCompliance***

#### **FINDING 05-JUST-3: The Justice Cabinet Should Implement Procedures To Ensure Consistent Enforcement And Documentation Of Subrecipient Monitoring Requirements (Continued)**

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##### **Management's Response and Corrective Action Plan (Continued)**

*Byrne grants managed by the Office of the Secretary are also "participating" in MARS and required to report financial information on a quarterly basis. Deficiency notices were sent to the Office of the Secretary for missing financial reports; unfortunately, due to staffing limitations, grant reports were not completed (and, therefore, reviewed), until the grant close out. The Office of the Secretary will strive to improve reporting in the future, and Grants Management Branch will assist in this process whenever possible.*

*Regarding A-133 certification of 2004 VAWA applications, the certification page was erroneously left out of mailed hardcopy grant applications. It has been included in prior and subsequent years for all grant applications for federal funds issued by Grants Management Branch and will continue to be. It should be noted that 29 of 34 VAWA grant applications received during the 2004 application cycle were for continuation projects. Fiscal staff, therefore, was already well acquainted with the majority of applicants' source and scope of funds and prior years' A-133 status. Additionally, all grant applications received included audits (as recorded in GMB's database) and these were reviewed for A-133 status, findings, and related issues.*

#### **FINDING 05-JUST-4: The Justice Cabinet Should Agree Federal Expenditure Reports To MARS**

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State Agency: Justice Cabinet - Office of the Secretary

Federal Program: CFDA 16.575--Crime Victim Assistance

CFDA 16.579--Byrne Formula Grant Program

CFDA 16.588--Violence Against Women Formula Grants

Federal Agency: U.S. Department of Justice - Office of Justice Programs

Pass-Through Agency: Not Applicable

Compliance: Reporting

Amount of Questioned Costs: None

During fiscal year 2005, Grants Management Branch (GMB) closed out their 2001 VOCA and 1999 VAWA awards. Auditors reviewed the closeout SF-269 reports submitted for these closed grants and found that for the 2001 VOCA-5TA01 grant, federal expenditures reported did not reconcile to Kentucky's accounting system, MARS (Management Administrative Reporting System). GMB reported \$5,248,034 of expenditures in their

**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Reportable Conditions Relating to Internal Control and/or Reportable  
Instances of NonCompliance*****FINDING 05-JUST-4: The Justice Cabinet Should Agree Federal Expenditure  
Reports To MARS (Continued)**

---

final FS-269 and received reimbursement for this amount. However, actual MARS expenditures for the grant were \$5,273,000, a difference of \$24,966. Since the grant had been closed when this error was discovered, Kentucky has lost \$25,000 in Federal reimbursement.

Auditors also reviewed all SF-269 reports filed for the quarter ended March 31, 2005 for all 16 open grants for VAWA, VOCA and BYRNE.

- Auditors were able to agree cumulative federal expenditures reported on the SF-269 reports to MARS for only four (4) grants.
- There is no documentation of the supervisor's review of the SF-269 reports.

Additionally, project-billing errors did not allow expenditures from certain grant projects to be included in calculations used to determine federal drawdowns. As a result, Kentucky had not been reimbursed for \$1.9 million dollars of federal expenditures at the end of the 2005 fiscal year. These funds were received in FY 2006 when the project billing errors were corrected.

Errors in federal reporting were the result of accounting entry errors made over the past several years when GMB did not have adequate controls over accounting entries to prevent improper coding of accounting entries. These errors have been corrected but were not detected prior to the close of the VAWA 1999 and VOCA 2001 grants during fiscal year 2005.

Billing errors resulted from changes made to the project billing tables in MARS, which caused expenditures to not be included in drawdowns. This problem was exacerbated by the failure of GMB to compare or review expenditure and revenue reports, which would have made GMB aware of the problem

According to the U.S. Department of Justice Financial Guide, Chapter 11: Reporting Requirements, "These reports will contain the actual expenditures and unliquidated obligations as incurred (at the lowest funding level) for the reporting period (calendar quarter) and cumulative for the award. The award recipients will report program outlays and revenue on a cash or accrual basis in accordance with their accounting system."

**Recommendation**

GMB has already implemented changes to resolve problems that led to the reporting and billing errors.

- A new grant accountant has been hired with duties including the approval and review of grant expenditures and federal reporting.

## **FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

### ***Reportable Conditions Relating to Internal Control and/or Reportable Instances of NonCompliance***

#### **FINDING 05-JUST-4: The Justice Cabinet Should Agree Federal Expenditure Reports To MARS (Continued)**

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##### **Recommendation (Continued)**

- New procedures have been implemented for the payment of subrecipients to prevent coding of expenditures to the wrong grant year.
- Grant expenditures are reviewed prior to initiating the drawdowns to ensure that all eligible expenditures have been accrued for the draw.
- The grant accountant is continuing the process of correcting errors to the grants with the goal of having all errors corrected by the end of the 2006 fiscal year and the implementation of the state's new accounting system.

We recommend that GMB continue with the process of documenting and correcting past accounting entry errors. This should include a review of drawdown activity to ensure that all available federal funds have been drawn down.

Federal reports should be corrected so that federal expenditures reported agree to federal expenditures as recorded in MARS.

##### **Management's Response and Corrective Action Plan**

*GMB will continue current documentation practices and corrections efforts. In addition, the Branch Manager will formally sign-off on SF269 forms in the future.*

#### **FINDING 05-JUST-5: The Justice Cabinet Should Not Supplant State Funds With Federal Funds**

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State Agency: Justice Cabinet - Office of the Secretary

Federal Program: CFDA 16.579--Byrne Formula Grant Program

Federal Agency: U.S. Department of Justice - Office of Justice Programs

Pass-Through Agency: Not Applicable

Compliance: Allowable Costs/Cost Principles

Amount of Questioned Costs: \$34,435

Supplanting means to deliberately reduce State or local funds because of the existence of Federal funds. For example, when State funds are appropriated (expended) for a stated purpose and Federal funds are awarded for that same purpose, the State replaces its State funds with Federal funds, thereby reducing the total amount available for the stated purpose.

**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Reportable Conditions Relating to Internal Control and/or Reportable  
Instances of NonCompliance*****FINDING 05-JUST-5: The Justice Cabinet Should Not Supplant State Funds With  
Federal Funds (Continued)**

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The Office of Drug Control Policy (ODCP) was created within the Justice and Public Safety Cabinet during the 2005 Fiscal Year as a result of the recommendations of the Lieutenant Governor's Drug Control Assessment Summit as contained in their final report issued August 24, 2004. As a part of the realignment the Kentucky Agency for Substance Abuse Policy (KYASAP) was transferred to the Justice Cabinet and incorporated into ODCP by executive order of the Governor in July 2004.

KYASAP directs the Champions Against Drugs and KYASAP grant programs, which are supported by Tobacco Settlement and General Funds.

In September of 2004, the Justice Cabinet began the process of applying for BYRNE grant funds to create an "organizational entity that can coordinate, monitor and evaluate a unified drug control policy for the entirety of state government as well as liaison with local governments, the federal government and private entities."

The initial funding request for ODCP was for \$140,000 and included an Executive Director, two (2) staff persons, a program evaluator, and office equipment/supplies. Because of their concerns that funding of ODCP could be perceived as supplanting, the Grants Management Branch (GMB) removed the two (2) staff persons from the final approved budget for the grant.

Primarily, FY 2005 charges to the ODCP grant were first paid with General Fund or Tobacco Settlement Funds and then transferred to the grant. This method of payment, which accounts for 66% of the ODCP expenditures, indicates that the Justice Cabinet had additional state funds available for the ODCP but chose to replace those state dollars spent with newly acquired federal funding. This is not the intention of the federal granting agency, which specifically prohibits supplanting in their Financial Management Guide.

Among the expenditures transferred to the ODCP grant were payroll charges for their Executive Director, who began her position in February of 2005. She succeeded the Interim Director who was paid with state funds.

By transferring charges to the BYRNE grant that were already expended with State funds, the Justice Cabinet is supplanting federal funds.

According to the Office of Justice Programs Financial Management Guide, Chapter 3: "Federal funds must be used to supplement existing funds for program activities and must not replace those funds that have been appropriated for the same purpose."

**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Reportable Conditions Relating to Internal Control and/or Reportable  
Instances of NonCompliance*****FINDING 05-JUST-5: The Justice Cabinet Should Not Supplant State Funds With  
Federal Funds (Continued)**

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The Omnibus Crime Control and Safe Streets Act of 1968, Public law 90-351, §501 et seq., codified as amended at 42 USC 3750 et seq., states “Funds may be used to provide additional personnel, equipment, facilities (including upgraded and additional Law Enforcement Crime Laboratories), personnel training and equipment for more widespread apprehension, prosecution and adjudication of persons who violate State and local laws relating to the production, possession and transfer of Controlled Substances and to improve the Criminal Justice System. Outlined in the Act are other specific purposes for which funds can be used. The Act restricts the use of these funds for supplanting State and local funds and land acquisition, and construction other than penal or correctional facilities.”

Edward Byrne Memorial State and Local Law Enforcement Assistance Program: Formula Grant Program Guidance, FY 2004 states, “Grant funds, which include matching funds, may not be used to replace state or local funds that would, in the absence of federal assistance, be available or forthcoming for law enforcement. Instead, grant funds must be used to increase the total amount of such other funds the grantee agency uses.”

**Recommendation**

We recommend that the Justice Cabinet reimburse the BYRNE Grant for the above-mentioned expenditures. We further recommend that the Justice Cabinet thoroughly review grant requirements to ensure they are in compliance with all federal grant regulations.

**Management’s Response and Corrective Action Plan**

*The Justice and Public Safety Cabinet disagrees with the finding of supplanting as described above. The mission and duties of the Office of Drug Control Policy is much broader than the KYASAP program that it absorbed responsibility for upon its creation. Also, the ODCP’s Interim Director position, and the currently staffed Executive Director position are distinct and separate in time, duties, and mission. Therefore, they do not reflect an issue of supplanting. Additionally, the referenced grant was issued prior to the expenditure of funds for, or the retention of the incumbent in, the current position. Due to staffing limitations in the Office of the Secretary, the grant was not immediately set up in MARS, resulting in salary charges being applied to general fund and later journal vouchered to federal funds. Expenditures were determined to be eligible and appropriate charges for the intended purpose of the grant and within the grant period by program and fiscal staff prior to the transfer.*

**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Reportable Conditions Relating to Internal Control and/or Reportable  
Instances of NonCompliance*****FINDING 05-JUST-5: The Justice Cabinet Should Not Supplant State Funds With  
Federal Funds (Continued)**

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**Auditor's Reply**

We reaffirm our position that the ODCP grant supplanted available state funding with federal funding. Changing the funding of the executive director's position from state funds to federal funds falls within the federal definition of supplanting. Despite a change in mission from the interim director to the current executive director position, the Justice Cabinet had funds available for the director's position and shifted those costs to the BYRNE grant.

**FINDING 05-JUST-6: The Justice Cabinet Should Ensure That All Equipment Is  
Properly Entered Into MARS**

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State Agency: Justice Cabinet - Office of the Secretary

Federal Program: CFDA 16.579--Byrne Formula Grant Program

Federal Agency: U.S. Department of Justice - Office of Justice Programs

Pass-Through Agency: Not Applicable

Compliance: Equipment and Real Property Management

Amount of Questioned Costs: None

During FY 2005, \$19,958.75 of grant funds were used to purchase equipment and furniture including five (5) computers (\$5,210). We reviewed assets listed for the Justice and Public Safety Cabinet in MARS and found that these computers had not been added to the inventory, which is contrary to federal and state requirements/regulations.

After inquiry, these computers were added into MARS. However, they were not added with the correct funding information. While the computers were originally purchased with the cabinet's General Fund appropriation, GMB transferred the expenditures via a Journal Voucher (JV) to the ODCP Byrne grant two (2) weeks later and the funding for these assets should reflect this change.

As of March 10, 2006, Justice Cabinet's Office of the Secretary (Agency 500) had not input any additions of equipment or vehicles with an acquisition date after October 29, 2003 into the MARS Advantage tables. The Office of the Secretary purchased \$272,554 of equipment and furniture during FY 2005. Because records were not updated, it is not possible to determine the exact dollar amount of equipment that exceeded the \$500 threshold requiring entry to MARS.



**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Reportable Conditions Relating to Internal Control and/or Reportable  
Instances of NonCompliance*****FINDING 05-JUST-6: The Justice Cabinet Should Ensure That All Equipment Is Properly Entered Into MARS (Continued)**

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Failure to follow Finance and Administration Cabinet policies and procedures regarding the input of assets has resulted in an incomplete inventory record for the Office of the Secretary. This violates federal grant requirements relating to maintenance of records for purchases of equipment with grant funds in accordance with applicable state laws/regulations.

Office of Justice Programs Financial Management Guide, Chapter 6 states, “A subrecipient or State shall use and manage equipment in accordance with its procedures as long as the equipment is used for criminal justice purposes.”

OMB Circular A-133 states, “A State shall use, manage, and dispose of equipment acquired under a Federal grant in accordance with State laws and procedures.”

Finance and Administration Cabinet’s Fixed Assets Policies and Procedures state that, “The Finance and Administration Cabinet (FAC) has existing regulations, as well as policies and procedures, governing the purchase and management of the Commonwealth’s fixed assets. Agencies are required to properly account for all fixed asset transactions that meet or exceed the statutory threshold. KRS 45.313 states: “Each budget unit shall maintain a current inventory of equipment having an original cost of five hundred dollars (\$500) or more. The inventory shall be available for examination by the Finance and Administration Cabinet at all times.” All agencies are responsible for managing their fixed assets in accordance with this statute, as well as complying with all state and federal regulations.

The ADVANTAGE Fixed Asset Module must be used for the tracking of all state assets with a cost of \$500 or more. This is not an option as FAP 120-20-01 states: “Agencies shall enter records into the fixed asset system for non-expendable property that promotes financial reporting, safeguarding of assets, and adequate insurance.” The fixed asset system referred to in FAP 120-20-01 is the MARS ADVANTAGE Fixed Asset Module. Assets are generally defined as non-expendable items having a useful life of more than one year and a cost of five hundred dollars (\$500) or more.”

**Recommendation**

The Justice Cabinet should review purchase records in FY 2004 and FY 2005 to ensure that all equipment with a value exceeding \$500 and with an expected useful life exceeding one (1) year has been updated to the MARS/Advantage tables as required by FAP 120-20-01.

Further, Justice should ensure that future purchases are added to the MARS/Advantage tables in a timely manner as they are acquired.

**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Reportable Conditions Relating to Internal Control and/or Reportable  
Instances of NonCompliance*****FINDING 05-JUST-6: The Justice Cabinet Should Ensure That All Equipment Is Properly Entered Into MARS (Continued)**

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**Management's Response and Corrective Action Plan**

*The Justice and Public Safety Cabinet acknowledges the validity of the finding that during FY 05 five computers were purchased for the Office of Drug Control (ODC) in the total amount of \$5,210.*

*Further, the computers were identified and located by the agency accessing the internal agency records which at that time did not include the entries of fixed asset data in the MARS ADVANTAGE tables as required for compliance with state and federal regulations.*

*Documents associated with the purchase of the computers did/does reflect the purchase being made with agency funds without the realization that charges had been eventually transferred to federal funds.*

*Even though all FA shells have not been completed in the MARS electronic system since October 29, 2003 as indicated in the report, many shells consists of purchases for laboratory chemicals and supplies which are not of inventory nature which simply need to be deleted. Copier lease payments are also inclusive in the FA documents which are not considered to be agency inventory. These too will need to be deleted. Once those type deletions are made, the total purchases made as indicated (\$272,554) will/should be reduced significantly.*

*Planned Course of Action by Agency:*

*Due to the tremendous growth of the agency and the increase of responsibilities during the last 24-36 months, the agency has not intentionally neglected policies and procedures relating to maintenance of documents and records as required in accordance with applicable state and federal laws/regulations. To the contrary, it has been faced with the multiple tasks of developing/implementing procedures offering accountability and compliance as required without the availability of any additional staff in order to meet these demands.*

*Several weeks ago, the agency devised a plan to "decentralize" various fiscal and/or administrative tasks and delegate a degree of responsibility back to the Division/Unit within the Cabinet. Through the decentralization process, the FA documents will be completed by the Division/Unit associated with the acquisition of the property promptly after payment has been made for the purchase. The inventory roll-up documents/records will be maintained at the Central Administrative Office by the fiscal manager. This plan cannot become effective until after July, 2006. (See further explanation in remaining response)*

**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Reportable Conditions Relating to Internal Control and/or Reportable  
Instances of NonCompliance*****FINDING 05-JUST-6: The Justice Cabinet Should Ensure That All Equipment Is  
Properly Entered Into MARS (Continued)**

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**Management's Response and Corrective Action Plan (Continued)**

*As always needed, keeping the communication lines open from office to office will be strongly encouraged to allow for any changes/modifications that may be necessary before final filing of the document.*

*Currently, the agency has only 2 staff members who can assist with the creation of FA documents and one currently being trained available to assist on a part-time basis. Through these 2.5 individuals, the Justice Cabinet shall review purchase records in FY 2004 and FY 2005 to ensure that all equipment with a value exceeding \$500 and with an expected useful life exceeding one year has been updated to the MARS Advantage tables as required by FAP 120-20-01. This activity is scheduled to be concluded by mid-May.*

*The additional staff designated to be trained at the Division/Unit level resulting from the decentralization plan can not be scheduled for necessary training as needed until classes are open and available after July 1, 2006. This occurrence is due to the implementation of the eMARS system, which does not include scheduled training for new users until the implementation process has been completed.*

*The Justice and Public Safety Cabinet, Office of Management and Administrative Services further commits to ensure that future purchases shall be made to existing MARS/EMARS tables in a timely manner as they are acquired when all conditions are within agency control.*

**SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS  
FOR THE YEAR ENDED JUNE 30, 2005**

<b>Fiscal Year</b>	<b>Finding Number</b>	<b>Finding</b>	<b>CFDA Number</b>	<b>Questioned Costs</b>	<b>Comments</b>
<b><u>Reportable Conditions</u></b>					
<i>(1) Audit findings that have been fully corrected:</i>					
FY 04	04-JUST-3	The Justice Cabinet Should Monitor Grant Funds Passed-Thru To Other State Agencies For Compliance With Grant Requirements	16.579	\$0	Resolved. Agencies repaid questioned amounts. No exceptions noted during FY 05 testing.
<i>(2) Audit findings not corrected or partially corrected:</i>					
FY 04	04-JUST-1	The Justice Cabinet Should Implement And Follow An Approved Indirect Cost Allocation Plan	16.575 16.579 16.588	\$363,063	Partially Resolved. While USDOJ has determined an indirect cost plan is not required, they have requested documentation of the Justice Cabinet's indirect cost allocation method. See 05-JUST-2.
FY 04	04-JUST-2	The Justice Cabinet Should Provide Sufficient Documentation Of Subrecipient Monitoring Activities	16.575 16.579 16.588	N/A	Not Resolved. Exceptions noted during FY 05 testing. See 05-JUST-3.
FY 04	04-JUST-4	The Justice Cabinet Should Implement Procedures To Ensure All Grant Funds Are Expended In Accordance With Federal Guidelines	16.575 16.579 16.588	N/A	Not Resolved. Testing indicates that intra-agency grant recipients did not comply with Justice Cabinet requirements for subrecipients. See 05-JUST-3.

**SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS  
FOR THE YEAR ENDED JUNE 30, 2005**

<b>Fiscal Year</b>	<b>Finding Number</b>	<b>Finding</b>	<b>CFDA Number</b>	<b>Questioned Costs</b>	<b>Comments</b>
<b>Reportable Conditions (Continued)</b>					
<b>(2) Audit Findings Not Corrected or Partially Corrected (Continued):</b>					
FY 04	04-JUST-5	The Justice Cabinet Should Not Supplant State Funds With Federal Funds	16.579	\$30,413	Partially Resolved. Questioned costs repaid. Supplanting found again FY 05. See 05-JUST-5.
FY 03	03-JUST-1	The Justice Cabinet Should Either Develop An Indirect Cost Allocation Plan And Submit It To The Cognizant Federal Agency For Approval Or Stop Charging Indirect Costs To The Federal Government	16.575 16.579 16.588	\$46,774	Partially Resolved. While USDOJ has determined an indirect cost plan is not required, they have requested documentation of the Justice Cabinet's indirect cost allocation method. See 05-JUST-2.
FY 03	03-JUST-2	The Justice Cabinet Should Follow Established Subrecipient Monitoring Policies And Procedures To Ensure Subrecipient Monitoring Is Properly Performed And Documented	16.575 16.579 16.588	N/A	Not Resolved. Subrecipient monitoring procedures improved, but exceptions noted during FY 05 testing. See 05-JUST-3.
FY 03	03-JUST-4	The Justice Cabinet Should Ensure Information On The Quarterly Financial Status Report Is Reliable	16.575 16.579 16.588	N/A	Not Resolved. Exceptions noted during FY 05 Testing. See 05-JUST-4.
FY 02	02-JUST-2	The Justice Cabinet Should Develop Written Subrecipient Monitoring Policies and Procedures to Ensure Subrecipient Monitoring Is Properly Performed And Documented	16.575 16.579 16.588	N/A	Partially Resolved. Exceptions noted during FY 05 testing. See 05-JUST-03.

**SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS  
FOR THE YEAR ENDED JUNE 30, 2005**

<b>Fiscal Year</b>	<b>Finding Number</b>	<b>Finding</b>	<b>CFDA Number</b>	<b>Questioned Costs</b>	<b>Comments</b>
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**Reportable Conditions (Continued)**

***(2) Audit Findings Not Corrected or Partially Corrected (Continued):***

FY 02	02-JUST-4	The Justice Cabinet Should	16.575	N/A	Not Resolved.
		Prepare Quarterly Financial	16.579		Exceptions noted
		Status Reports That Are	16.588		during FY 05 Testing.
		Supported By Adequate			See 05-JUST-4.
		Documentation			

***(3) Corrective action taken is significantly different from corrective action previously reported:***

There were no findings for this section.

***(4) Audit finding is no longer valid:***

There were no findings for this section.

**Material Weaknesses**

***(1) Audit findings that have been fully corrected:***

There were no findings for this section.

***(2) Audit findings not corrected or partially corrected:***

There were no findings for this section.

***(3) Corrective action taken is significantly different from corrective action previously reported:***

There were no findings for this section.

***(4) Audit finding is no longer valid:***

There were no findings for this section.

**Other Matters**

***(1) Audit findings that have been fully corrected:***

There were no findings for this section.

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**SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS  
FOR THE YEAR ENDED JUNE 30, 2005**

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<b>Fiscal Year</b>	<b>Finding Number</b>	<b>Finding</b>	<b>CFDA Number</b>	<b>Questioned Costs</b>	<b>Comments</b>
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**Other Matters (Continued)**

***(2) Audit findings not corrected or partially corrected:***

FY 04	04-JUST-6	The Justice Cabinet Should	16.575	N/A	Not resolved. FY 05 reports not supported by adequate documentation. See 05-JUST-4.
		Ensure That Information	16.579		
		On The Quarterly	16.588		
		Financial Status Report Is Supported By Adequate Documentation			

***(3) Corrective action taken is significantly different from corrective action previously reported:***

There were no findings for this section.

***(4) Audit finding is no longer valid:***

There were no findings for this section.